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In the Literature

Highlights from Commonwealth Fund-Supported Studies in Professional Journals

Strained Local and State Government Finances Among Current Realities That Threaten Public Hospitals' Profitability

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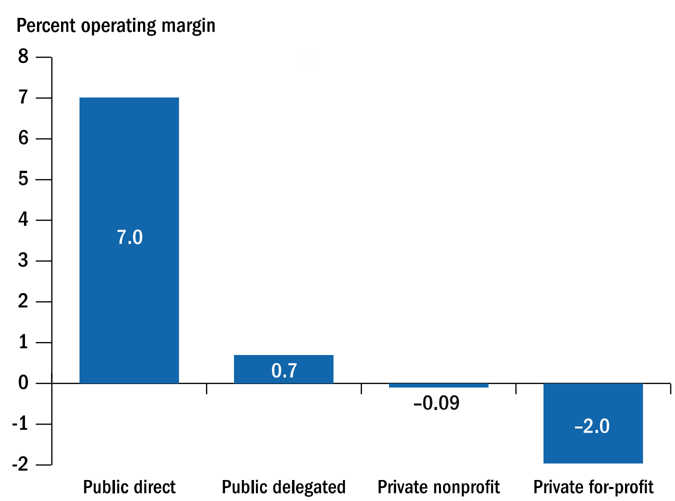
Synopsis

Prior to the 2008–09 economic recession, safety-net hospitals that were directly governed by elected officials and in highly competitive markets had significantly higher operating margins than more politically independent safety-net hospitals. Because their better performance was tied to government subsidies rather than superior financial controls, these hospitals will face significant financial reversals if they fail to change their business practices before the Affordable Care Act's scheduled reduction in subsidies takes effect and a weak economy forces further cutbacks.

Operating Margins of Safety-Net Hospitals by Governance Type, 2003–2007



Source: Adapted from N. M. Kane, S. J. Singer, J. R. Clark et al., "Strained Local and State Government Finances Among Current Realities That Threaten Public Hospitals' Profitability," *Health Affairs*, Aug. 2012 31(8):1680–89.

The Issue

Safety-net hospitals play a vital role in serving uninsured and low-income populations, especially in large urban communities, but little is known about the factors that influence their financial viability. To identify these factors, the authors of this Commonwealth Fund–supported study compared the financial performance of 150 safety-net hospitals, examining governance type, financial performance, and market concentration, among other variables. To further clarify their findings, the authors conducted site visits at nine hospitals.

Key Findings

- The researchers segmented safety-net hospitals into four categories: public hospitals that are directly governed by elected officials; public hospitals with governing authority that has been delegated to political appointees; private, nonprofit hospitals; and private, for-profit hospitals. They found that safety-net hospitals governed directly by elected officials had the highest operating margins between 2003 and 2007 (7.0%), followed by public delegated ones (0.7%), nonprofit safety-net hospitals (–0.09%), and for-profit safety-net hospitals (–2.0%). However, the financial advantages of direct public governance were limited to the most competitive markets.
- Interviews with hospital leaders suggest the higher margins are linked to an ability to negotiate larger government subsidies. Some of the directly controlled hospitals and one of the delegated public authority hospitals the authors visited received local subsidies of between 25 percent and 35 percent of total revenues. In contrast, none of the private, nonprofit sites received local government subsidies. The site visits also revealed that private, nonprofit safety-net hospitals developed strong financial control systems and pursued strategies to attract insured patients.

Addressing the Problem

To overcome declining government subsidies, safety-net hospitals governed by elected politicians must focus on cost control, quality improvement, and services that attract insured patients. Such efforts will be important to ensure that the 23 million people who will be without insurance coverage even when the health reform law takes full effect—including illegal immigrants, people with chronic psychological illnesses, and those whose incomes are not high enough to afford private insurance—continue to receive the range of health care and specialized services, like transportation and language translation, that these hospitals provide.

About the Study

The authors examined five years' worth of financial data from 150 urban safety-net hospitals throughout the United States that met at least one of the following three criteria: a threshold percentage of Medicaid discharges, a threshold percentage of minority discharges, or 2007 membership in the National Association of Public Hospitals and Health Systems. They conducted site visits and interviewed board members, senior executives, managers, and other staff at nine hospitals.

The Bottom Line

Safety-net hospitals that currently rely on politically negotiated funding must adapt to increasing fiscal austerity and intensified competition by revamping their business strategies.

Citation

N. M. Kane, S. J. Singer, J. R. Clark et al., "Strained Local and State Government Finances Among Current Realities That Threaten Public Hospitals' Profitability," *Health Affairs*, Aug. 2012 31(8): 1680–89.

This summary was prepared by Sarah Klein.